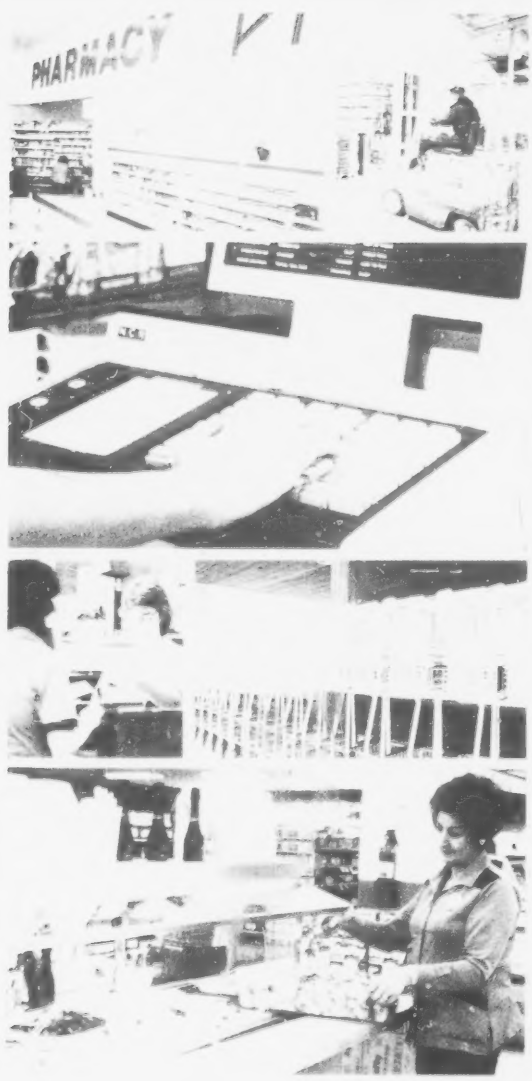
ANNUAL FINANCIAL REVIEW



The Annual Report of the Supermarket Industry

FOOD MARKETING INSTITUTE

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Conducted by:

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EXECUTIVE SUMMARY

The Food Marketing Institute ("FMI") has been tracking the performance of the supermarket industry for the past twelve years. The 1983 Annual Financial Review (the "Review") was designed to promote a better understanding of the economics of the supermarket industry. This report provides the broadest and most representative sample of the industry available. Data were collected from 148 companies operating a total of over 10,000 stores.

The Review was conducted for FMI by Gerke Economics, Inc. Information was derived from an extensive mail survey and from public financial reports.

The results of the Review indicate that while 1983 was a year of economic recovery, industry profits remained flat when compared to 1982. Net income as a percentage of sales was 1.05 percent in 1983 compared to 1.06 percent in 1982.

Profit performance varied by company size. The smaller companies showing a decline in net profit margin while the larger companies showed a slight increase when compared to 1982.

For several years the smallest companies experienced higher rates of profit than the larger firms. This year, however, the larger firms have slightly higher profits as a percent of sales although the smallest companies continue to lead in return on total assets (see page 7). The mid-sized firms continue to show lower profits than either the smaller or larger competitors.

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FINANCIAL DATA AND RATIOS

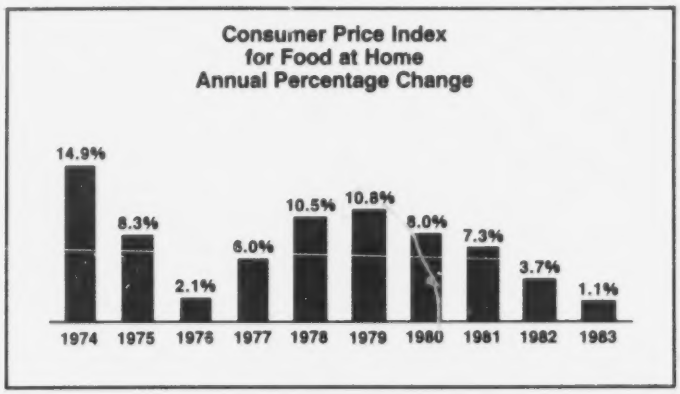
Selected Economic Data

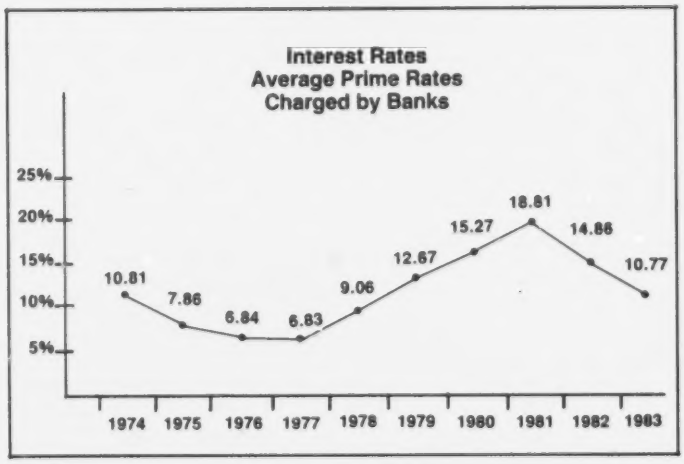
During 1983, the U.S. economy continued to recover from the most severe recession since the great depression.

Inflation, as measured by the consumer price index for all urban consumers was 3.2 percent, the lowest rate since 1967. The consumer price index for food-at-home rose a scant 1.1 percent.

Interest rates, having dropped considerably during 1982 held steady through 1983. The average monthly prime rate charged by banks ranged from 10.5% to 11.3%.

With inflation at about 3 percent and the prime rate hovering around 11 percent, "real" interest rates in 1983 were considerably above historical levels.



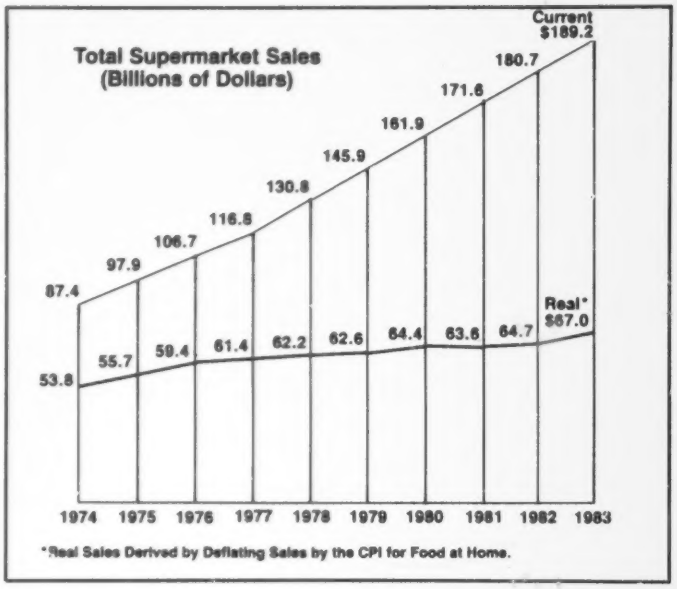


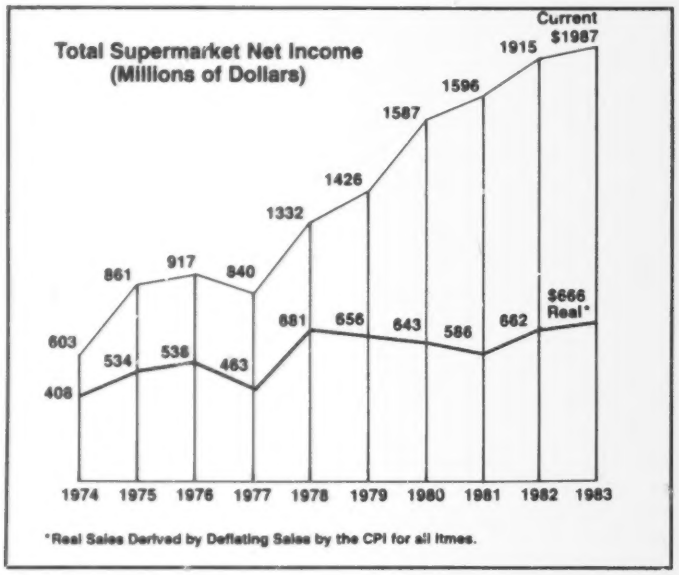
Industry Data*

As measured in current dollars, total supermarket sales continued their long-term growth and reached a record $189.2[1] billion in 1983. Total supermarket net income was almost $2.0 billion. Adjusted for inflation, total supermarket net income in real dollars was $666 million. This was an increase of less than one percent over 1982. And it fell far short of the record total of $681 million in 1978 when total supermarket net income exceeded the previous year by almost 50 percent. The 1983 increase was also significantly less than the regular annual increases of 20-30 percent experienced in the early 1970's.

[1]*Progressive Grocer*

**Total supermarket sales and net income were deflated by the Consumer Price Index that best reflects the underlying nature of the data. Since supermarket sales are composed primarily of food, the sales data were deflated by the CPI for "food-at-home." Since supermarket net income is composed of all revenue and expense accounts (many of which are not related to food), the net income data were deflated by the CPI for all items.*





Key Financial Ratios

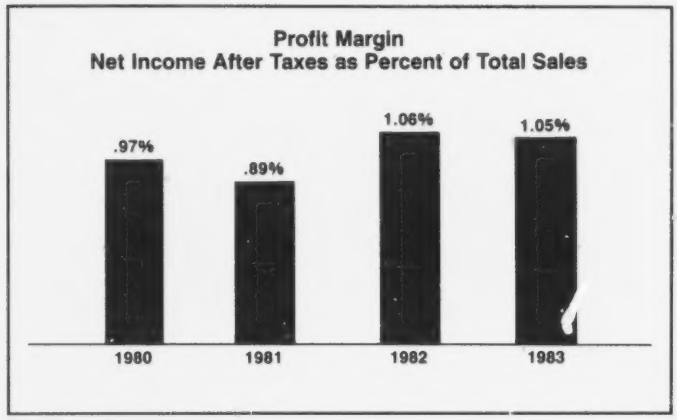
In measuring profitability, three financial ratios taken together provide a good overall picture of the industry:

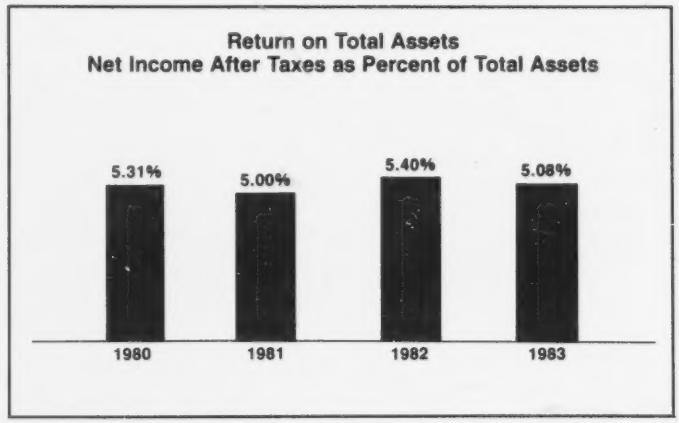
- profit margin
- return on total assets
- return on net worth.

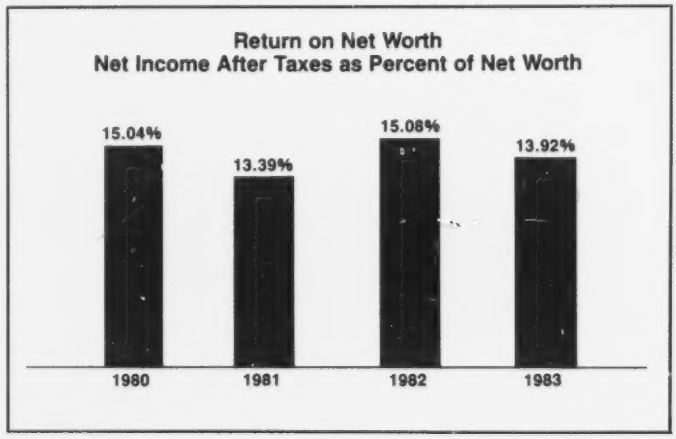
The profit margin is simply net income as a percentage of sales. It measures the portion of the industry's sales dollar that is left after paying all expenses, including the cost of the products. For the supermarket industry in 1983 the profit margin was 1.05 percent.

Return on total assets is calculated by expressing net income as a percentage of total assets. It measures the ability of the industry's combined equity and debt capital to generate profits. In 1983 the supermarket industry's return on total assets declined to 5.08 percent from 5.40 percent one year earlier.

Return on net worth is calculated by expressing net income as a percentage of net worth. It reflects the earning power of the stockholders' equity in the supermarket industry. Return on net worth in the supermarket industry was 13.92 percent in 1983, down from 15.08 percent for the previous year.





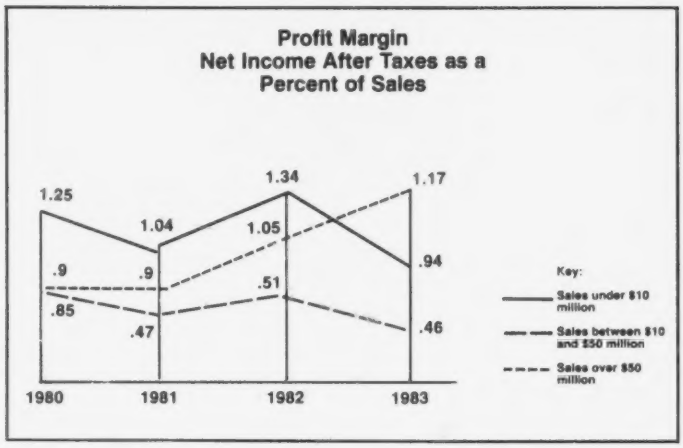


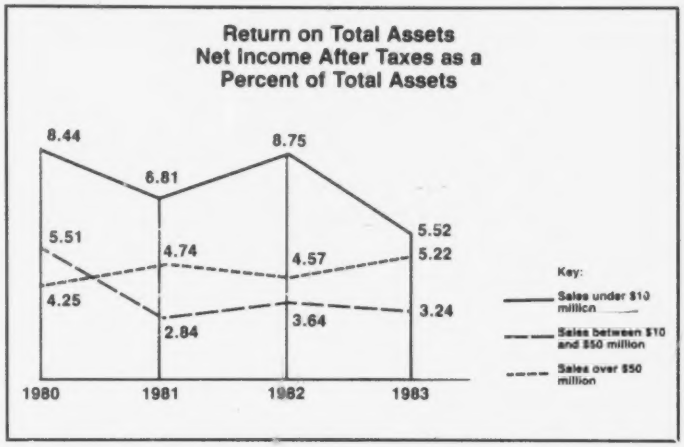
To provide a more complete understanding of the supermarket industry, profit ratios are reported for three size categories. The size categories are for firms which have annual sales of:

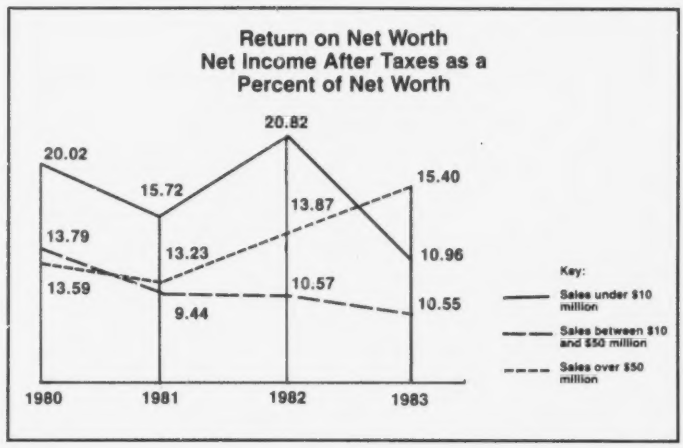
- less than $10 million
- $10-$50 million
- $50 million and more

From 1980 to 1982, the smallest firms enjoyed the greatest profitability. However, the financial picture changed during 1983. The largest firms showed a higher profit margin as well as a higher return on net worth, although the smallest firms did maintain their number one position in return on total assets.

As in the past, the mid-size firms had the lowest ranking in all three ratios.





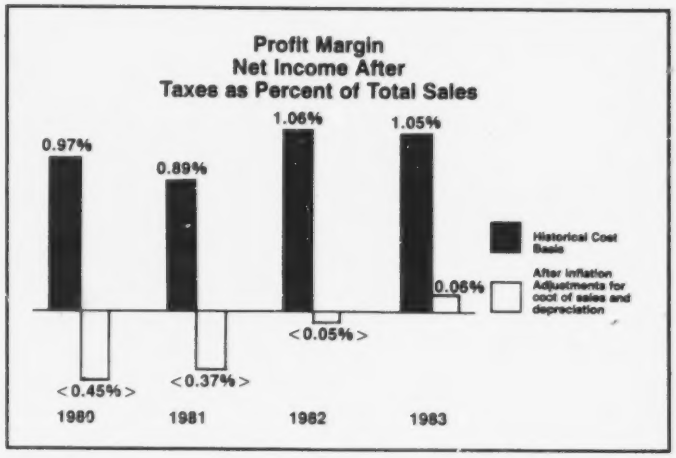


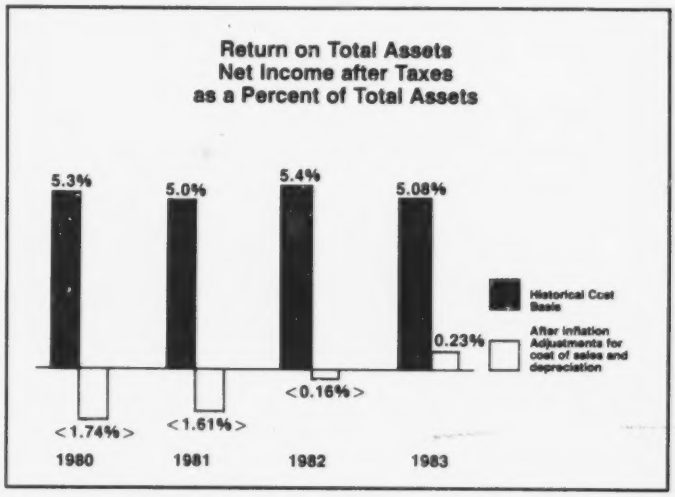
Key Financial Ratios Adjusted for Inflation

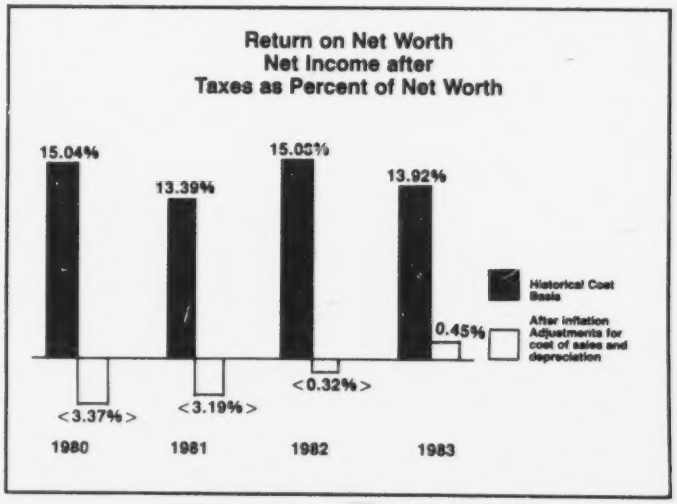
The performance measures discussed in the previous section are subject to distortion caused by inflation. For comparison, ratios are herein presented on an inflation-adjusted basis in order to more accurately reflect the economic well-being of the supermarket industry.

The inflation adjustments used in the Review are those prescribed by Statement of Financial Accounting Standards No. 33. Such adjustments restate "cost of sales" and "depreciation" from the amounts recorded in historical dollars to current dollars. In so doing, (1) the impact of profits realized on inventory are removed from the income statement, and (2) the depreciation charge is increased to reflect the current costs of replacing assets.

Low inflation in 1983 brought real growth to the supermarket industry. The inflation-adjusted ratios after several years of negative results finally turned positive in 1983. The profit margin, return on total assets and return on net worth were 0.06%, 0.23% and 0.45%, respectively.





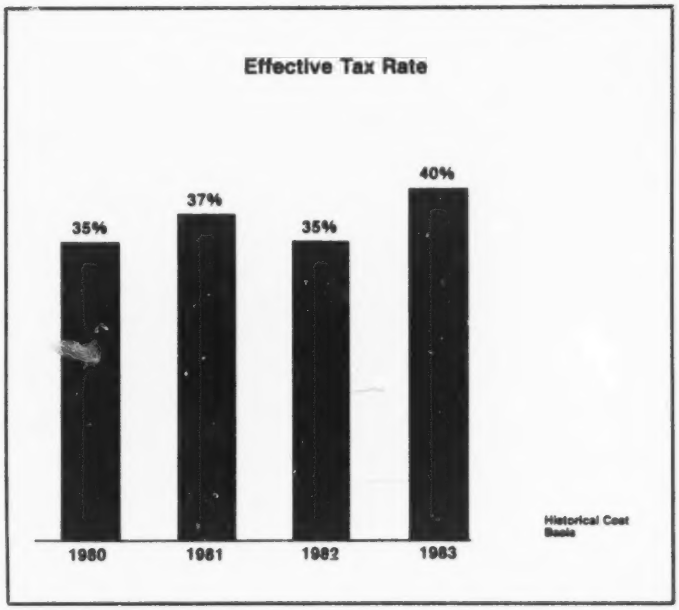


Tax Rates

Income Taxes

Income taxes impact corporations by consuming much, if not all, of their "real" pre-tax profits. Income tax calculations for an individual company are based upon net income calculated on an *historic* cost basis. For tax reporting, no adjustments are made to reflect the erosion of purchasing power that occurrs through inflation. For example, depreciation expense for equipment is based on its actual cost, rather than on the current cost of replacing it.

On this historic cost basis, 1983 income taxes paid by the supermarket industry were 40 percent of pre-tax profits, a significant increase from previous years.



Wage Taxes

In addition to taxes on income, supermarkets pay taxes based on wages. For the first time in this survey, companies listed FICA tax payments and Unemployment Compensation payments. In 1983 FICA tax payments amounted to 0.77 percent of sales. Unemployment Compensation payments were 0.17 percent of sales.

Given that the industry sales are $189.2 billion, the supermarket industry in 1983 paid out $1.5 billion in FICA payents and $321 million in Unemployment Compensation payments.

FINANCIAL STATEMENTS

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Year Summary

Income Statement

The account balances in the income statement presented below have been expressed as percentages of sales, on an historic cost basis.

Income Statement for the Supermarket Industry
(In Percentages; Sales = 100%)

	1980	1981	1982	1983
Sales	100.00%	100.00%	100.00%	100.00%
Cost of Sales and Operating Expenses	98.20	98.62	98.24	98.23
Interest Expenses	.60	.51	.48	.46
Total Costs & Expenses	98.80	99.13	98.72	98.69
Operating Income	1.20	.87	1.28	1.31
Other Income	.36	.55	.34	.42
Income before Taxes	1.56	1.42	1.62	1.73
Total Taxes on Income	.55	.53	.57	.70
Extraordinary Items (Net)	(.04)	—	.01	.02
NET INCOME	.97%	.89%	1.06%	1.05%

Balance Sheet

The account balances in the balance sheet presented below have been expressed as percentages of total assets, on an historic cost basis.

End-of-Year Balance Sheet for the Supermarket Industry
(In Percentages; Total Assets = 100%)

ASSETS	1980	1981	1982	1983
CURRENT ASSETS				
Cash	6.86%	8.03%	7.10%	5.82%
Accounts Receivable	3.65	4.12	3.80	4.13
Marketable Securities	3.13	2.72	3.26	2.56
Inventory (Note A)	35.26	35.10	33.29	34.66
Other Current Assets	3.31	2.53	4.38	4.00
Total Current Assets	52.21	52.50	51.83	51.17
PROPERTY & EQUIPMENT (Note B)				
Land	2.32	2.30	2.32	2.75
Buildings	21.86	14.43	18.78	21.09
Fixtures & Equipment	39.73	40.94	40.83	42.89
Leasehold Improvements	7.29	9.62	7.30	8.97
Total Property & Equipment	71.20	67.29	69.23	75.70
Reserves for Depreciation	(28.51)	(26.01)	(29.33)	(32.84)
Net Property & Equipment	42.69	41.28	39.90	42.86
OTHER ASSETS	5.10	6.22	8.27	5.97
TOTAL ASSETS	100.00%	100.00%	100.00%	100.00%

NOTE A: Some firms value at least part of their inventory on a LIFO (last-in, first-out) basis. End-of-year inventories were recorded on a FIFO (first-in, first-out) basis for this report.

NOTE B: Property under capitalized leases is included in the appropriate property categories based on the type of property leased.

End-of-Year Balance Sheet for the Supermarket Industry
(In Percentages; Total Liabilities = 100%)

LIABILITIES & NET WORTH	1980	1981	1982	1983
CURRENT LIABILITIES				
Notes Payable	2.39%	2.23%	3.16%	2.43%
Accounts Payable	21.62	22.14	20.82	19.84
Income Taxes Payable	1.57	1.60	1.26	1.20
Other Current Liabilities	12.41	13.70	13.31	13.89
Total Current Liabilities	37.99	39.67	38.55	37.36
LONG-TERM DEBT				
Mortgages	6.50	3.81	5.38	4.57
Bank Loans	4.84	6.46	4.61	5.46
Bonds & Debentures	1.00	1.56	3.81	2.48
Capitalized Lease Obligations	9.37	6.83	7.50	7.86
Other Noncurrent Liabilities	2.75	3.14	3.00	2.53
Total Long-Term Debt	24.46	21.80	24.30	22.90
DEFERRED LIABILITIES	2.97	1.56	2.01	2.50
Total Liabilities	65.42	63.03	64.86	62.76
NET WORTH				
Common Stock Outstanding or Proprietorship	4.54	8.35	4.95	6.58
Preferred Stock Outstanding	.80	1.05	.96	.15
Paid-in Surplus	5.74	6.32	5.81	4.34
Retained Earnings	24.17	22.72	24.79	27.54
Treasury Stock	(.67)	(1.47)	(1.37)	(1.37)
Total Net Worth	34.58	36.97	35.14	37.24
TOTAL LIABILITIES & NET WORTH	100.00%	100.00%	100.00%	100.00%

Historical vs. Inflation-Adjusted Balance Sheet Categories

Certain balance sheet captions were grouped in categories, which have been expressed as percentages of total assets, in both historical dollars and inflation-adjusted dollars. The most significant impact of the inflation adjustments was to restate (i.e. increase) the value of "net property and equipment" in current year dollars. (This increase was also added to "net worth.") These adjustments recognize that the current costs of reproducing existing supermarket properties are significantly higher than the depreciated historic cost. Investors in supermarket properties are unable to realize those gains unless the company is dissolved or sold.

Balance Sheet Categories as Percent of Total — Historic Cost Basis

	1980	1981	1982	1983
Assets				
Inventory	35%	35%	33%	35%
Other Current Assets	17	18	19	16
Net Property & Equipment	43	41	40	43
Other Assets	5	6	8	6
Total	100%	100%	100%	100%
Liabilities and Total Net Worth				
Current Liabilities	38%	40%	39%	37%
Long Term Liabilities	27	23	26	26
Net Worth	35	37	35	37
Total	100%	100%	100%	100%

Balance Sheet Categories as Percent of Total — Adjusted for Inflation

	1980	1981	1982	1983
Assets				
Inventory	28%	28%	26%	26%
Other Current Assets	12	11	12	13
Net Property & Equipment	56	57	57	56
Other Assets	4	4	5	5
Total	100%	100%	100%	100%
Liabilities and Net Worth				
Current Liabilities	30%	32%	29%	28%
Long Term Liabiilities	22	18	22	21
Net Worth	48	50	49	51
Total	100%	100%	100%	100%

METHODOLOGY

Approach

The Review was developed from two primary sources of data: a survey mailed to the members of FMI and annual reports filed with the SEC on FORM 10-K.

For 1983, most of the financial data were supplied by the companies that responded to the survey. Data were not used for any company with sales of less than $2 million per store. Financial data for several large publicly traded companies were obtained from annual reports filed with the SEC. In all, data were collected from 148 companies that operated 10,335 stores. These firms accounted for sales of $91 billion.

The firms were separated into three size categories based on annual sales — companies with less than $10 million, companies with $10 to $50 million and companies with $50 million and over.

In order to develop the industry averages reported, means were calculated for each strata (size category) and were weighted using data from the 1977 Census of Retail Trade. The Census data are shown in the table below. The stratification and weighting of data help eliminate year-to-year changes that result from changes in the sample of firms submitting surveys.

We believe this method of estimating financial data for the supermarket industry provides the best published measurement of trends in the industry's capital structure. It does not, however, totally eliminate the problems of changes in sample size, varying fiscal year ends and supermarket operations in a diversified company.

Supermarket Population Based on 1977 Census of Retail Trade*

Firm Sales (Millions)	% of Total Firms	1977 Sales (Millions)	% of Total Sales
Less than $100	92.9%	$ 27,832	22.2%
Between $10 and $50.0	5.3%	12,800	10.2%
$50.0 and over	1.8%	84,823	67.6%
	100.0%	$125,445	100.0%

*Source: U.S. Census Bureau (latest available data)

Inflation Adjustments

The Financial Accounting Standards Board (the "FASB") has recognized that financial statements prepared on the basis of historical costs may not be meaningful in times of rapid inflation. As a result, Statement of Financial Accounting Standards No. 33 requires large companies to present data which reflect the impact of inflation. One method prescribed in SFAS No. 33 is to adjust cost of sales and depreciation from the amounts recorded in historical dollars to current year dollars. This approach, called constant dollar accounting, removes the effect of inventory profits on cost of sales from the income statement, and increases the depreciation charge to amounts reflective of the current cost of replacing assets. The Consumer Price Index for All Urban Consumers is used to make such adjustments.

After adjusting for the effects of inflation on cost of sales and depreciation, the industry has shown significant losses over the last several years. Reflecting the decreased rate of inflation, the industry actually showed a slight profit in 1983.

Net Income for the Supermarket Industry Adjusted for Inflation
(Expressed as a Percent of Sales)

	1980	1981	1982	1983
Net income, as reported	.97 %	.89 %	1.06 %	1.05 %
Adjustments to reflect the impact of inflation on:				
Cost of sales	(.82)	(.62)	(.28)	(.27)
Depreciation	(.60)	(.68)	(.83)	(.72)
Net income adjusted for inflation	(.45)%	(.37)%	(.05)%	.06 %

It is important, however, to consider one additional element during periods of inflation - gain or loss in purchasing power. In times of inflation, businesses that hold cash are at a disadvantage in terms of general purchasing power because their cash will buy less at the end of the period than at the beginning. On the other hand, entities that have debts during inflationary periods may gain an advantage because their debts will be repaid with dollars of lower purchasing power. Statement of Financial Accounting Standards No. 33 requires that the net of these gains and losses be disclosed separately from income from continuing operations. This separate disclosure requirement reflects the FASB's concern that a company can gain from borrowing. (The FASB believed that a gain in purchasing power associated with debt is a sign of successful management only when the funds have been invested in assets that maintain their purchasing power.) As a result, the gains in purchasing power that the supermarket industry has realized on monetary items have not been reflected in the inflation-adjusted data that have been previously presented in this report. These data, however, have been included in the following table.

Net Income for the Supermarket Industry Adjusted for Inflation (Expressed as a Percent of Sales)

	1980	1981	1982	1983
Net income, as reported	.97 %	.89 %	1.06 %	1.05 %
Adjustments to reflect the impact of inflation on:				
Cost of sales	(.82)	(.62)	(.28)	(.27)
Depreciation	(.60)	(.68)	(.83)	(.72)
Purchasing power	.96	.69	.50	.24
Net income adjusted for inflation and purchasing power	.51 %	.28 %	.45 %	.30 %

Definitions

Balance Sheet Captions

INVENTORY includes all goods held for sale by supermarket companies.

OTHER CURRENT ASSETS include all assets (except inventory) with a defined life of less than one year. (e.g., cash, accounts receivable, prepaid expenses, short-term investments, etc.)

NET PROPERTY & EQUIPMENT is all property, plant and equipment, including capital leases, less accumulated depreciation and amortization.

OTHER ASSETS include all assets (except property and equipment) with a defined life greater than one year. (e.g., investments in other companies, long-term receivables, etc.)

CURRENT LIABILITIES include all debts and expenses which are due within one year. (e.g., accounts payable, accrued liabilities, current portions of long-term debt, etc.)

LONG-TERM LIABILITIES include all debts and expenses which are due after one year. (e.g., long-term debt, capital lease obligations, deferred taxes, etc.)

NET WORTH is merely the difference between total assets and total liabilities. It is typically comprised of stock, paid-in-surplus, retained earnings and treasury stock.

Income Statement Captions

SALES represent all sales reported by supermarket companies

COST OF SALES AND OPERATING EXPENSES include the cost of merchandise sold by supermarkets plus all the other expenses of operating the stores, distribution facilities, and the central office.

INTEREST EXPENSE includes all interest charged on short- or long-term debt and on capital lease obligations.

OTHER INCOME includes all non-operating income (e.g., interest income, gain on sale of securities, etc.)

TOTAL TAXES ON INCOME are the Federal and state taxes imposed on the supermarket companies which are based on net income as reported to the government.

EXTRAORDINARY ITEMS include all items which occur infrequently and are unusual in nature (e.g., provisions for the disposition of facilities, realization of tax loss carry forwards, etc.)

Ratios

PROFIT MARGIN is the ratio of net income to sales.

RETURN ON TOTAL ASSETS is the ratio of net income to total assets.

RETURN ON NET WORTH is the ratio of net income to net worth.

Inflation Adjustments

INFLATION ADJUSTED NET INCOME is equal to net income as reported in historical dollars, less "constant dollar" adjustments to reflect the impact of inflation on (1) cost of sales, (i.e., to remove the effect of inventory profits from cost of sales) and (2) depreciation (i.e., to increase the depreciation charge to reflect the current cost of replacing assets.)

CONSTANT DOLLAR ACCOUNTING is a method of reporting financial elements in dollars which have the same general purchasing power.

MONETARY ITEMS are assets or liabilities which will be realized or paid for in cash for the exact amount of the amounts recorded on the balance sheet.

NON-MONETARY ITEMS are assets or liabilities which cannot be converted directly to cash for the amount recorded on the balance sheet. (e.g., inventory, property and equipment, deferred credits, etc.)

PURCHASING POWER GAIN OR LOSS is found by restating in constant dollars the (1) opening and closing balances of monetary assets and liabilities, and (2) transactions in monetary assets and liabilities.

The Food Marketing Institute (FMI) is a non-profit association that conducts programs in research, education and public affairs on behalf of its 1,300 members—food retailers and wholesalers and their customers in the United States and overseas. FMI's domestic member companies operate over 17,000 retail food stores with a combined annual sales volume of $130 billion—half of all grocery sales in the United States. More than three-fourths of FMI's membership is comprised of independent supermarket operators or small regional firms. Its international membership includes more than 100 members from 40 nations.